



## Don't Foreclose on Your Future!

Today's housing market is battling two ongoing problems: a long-lasting spike in foreclosures and millions of "underwater" mortgages—homes with mortgage balances that are higher than the homes are worth. According to a recent survey from zillow.com, nearly one in three homeowners with mortgages owe more than their homes are worth.

Compounding these issues is the phenomenon of "strategic" defaults. That means a homeowner who can pay his mortgage stops because he sees no reason to continue paying for an asset that is worth less than the debt it carries.

Almost 30% of foreclosures are so-called "strategic" defaults, and 27% of homeowners with negative equity would consider walking away from their mortgages if they faced financial trouble.

### Is Walking Away a Strategy?

Is it possible that many people are so shortsighted about the investment they've made in their homes?

Let's say a homeowner bought his home at the peak of the market in 2006 for \$220,000, the median home price that year. We'll say he put 5% down and got a 30-year mortgage for \$209,000. Now, fast-forward to 2012, when the median home price dropped to \$163,800.

If this is a fixed-rate mortgage at 6% interest, the balance in June 2012 was \$189,500. If our homeowner sells, he's lost his down payment plus more than five years of principal and interest payments, a total of \$93,700, and he still has to make up the \$25,700 difference between the selling price and the balance of the mortgage.

\$209,000 (original mortgage amount in 2006)

\$189,500 (mortgage balance in 2012)

-\$163,800 (home value in 2012)

\$25,700 underwater

The "wisdom" of the strategic default is to take the \$93,700 loss and save yourself the \$25,700 loss in home value by walking away instead of selling.

### Time for a Reality Check

Maybe, in some alternate reality, this is "wisdom." That alternate reality would have to be based on stagnant home values and banks that don't come after you for what you owe them. Let's try a true reality check:

Reality #1 – Your home is an investment, and any investment—even real estate—will go up and down in value. Walking away from your mortgage now is the equivalent of selling your stock portfolio at the bottom of the market. You guarantee yourself a loss if you don't stick with your investment until values come back up.

Reality #2 – Home values will recover. If our homeowner sticks it out and stays in his home, he'll be back to even in five years, based on a conservative 5% rate of appreciation. In less than 20 years, his home will have doubled in value. That is wisdom!

Reality #3 – The bank is not letting you off that easily. Lenders are covered up with foreclosures, so while homeowners who walk may not hear from the bank right away, they are by no means off the hook. Some banks will pull credit reports to see who is current on their other payments to determine if a default is "strategic." Banks will go to court to garnish wages or hijack tax refunds—whatever it takes to get what they're owed.

If you are truly unable to make your mortgage payments, you still should not walk away. You signed the contract, so you're under a moral obligation to pay. If you truly can't pay and keep food on the table, then it's time to talk with the bank about a possible short sale.

For expert help to buy or sell a home, work with one of Dave's real estate Endorsed Local Providers (ELPs). Your ELP will be able to advise you on your local market and help you buy or sell your home at the best price.

Stat sources:

<http://www.zillow.com/blog/2012-05-24/zillow-negative-equity-report-shows-1-in-3-mortgage-holders-underwater/>

<http://www.dsnews.com/articles/survey-more-underwater-homeowners-open-to-strategic-default-2011-05-13>